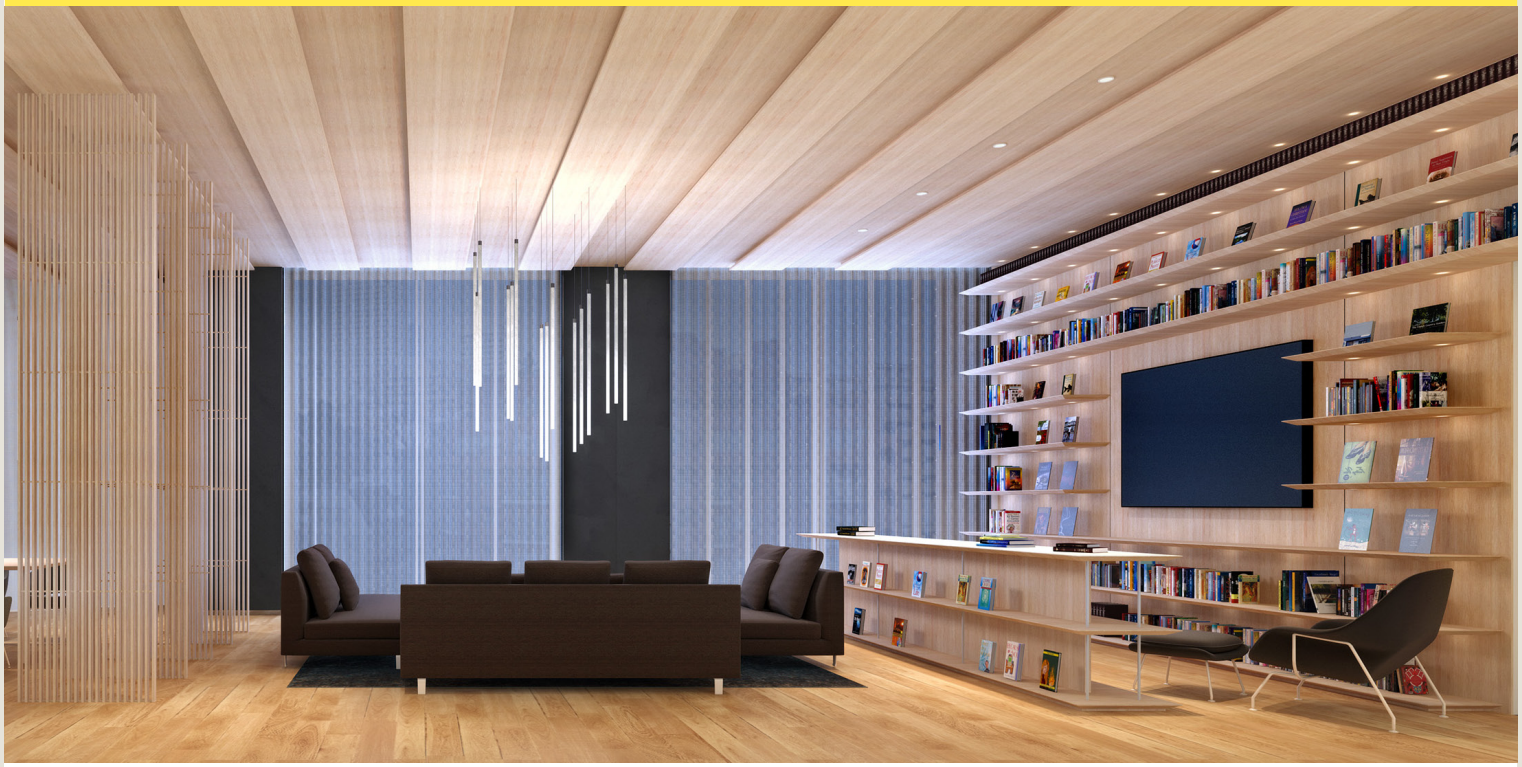
savills

Briefing
Residential leasing

Q3 2016



SUMMARY

Underlying fundamentals remain solid despite a pause in rental growth, indicating that the current gradual upward trend should not significantly change for the time being.

- Average mid-market asking rents in the 23-ward area stood at JPY3,624 per sq m (JPY11,980 per tsubo[1]), down 0.4% quarter-on-quarter (QoQ) but still up 0.3% year-on-year (YoY).
- After an impressive 3.0% gain in Q2 partially due to new building openings, rents in the central five wards corrected 1.1% QoQ to JPY4,217 per sq m (JPY13,941 per tsubo). They are still up 1.7% YoY.
- Tokyo's eastern wards have now seen the most growth in 2016, averaging 2-3% higher than a year ago.
- The highest rental premium against the 23-ward average was seen in the central five wards at 16.3%, while the Outer East continues to show the greatest discount at -22.5%.
- Though there have been minor fluctuations, average occupancy rates continue to remain above 95%.
- New residential housing starts in Tokyo have stabilised at approximately 140,000 units annually; however, we are seeing a gradual trend toward supplying more rental units and fewer units for other purposes.

"Mid-market asking rents in Tokyo's 23 wards saw mixed growth in Q3/2016, including some moderation after an especially strong Q2. Underlying fundamentals remain solid, however – occupancy has stayed above 95% in all survey areas." Savills Research & Consultancy

1 1 tsubo = approximately 3.306 sq m or 35.58 sq ft.

Savills Tokyo residential survey: Breakdown by geography

In order to illustrate trends in the central Tokyo residential market, Savills has segmented Tokyo's 23 wards into seven distinct geographical areas: Central (or "central five wards"), South, West, North (Inner and Outer) and East (Inner and Outer).

Savills rental index: Tokyo mid-market apartments

Savills collates over 20,000 leasing comparables each quarter in order to analyse trends affecting mid-market rental apartment units in Tokyo. Our benchmark rental data is based on average advertised monthly rents for units which fit the following criteria:

1) one- or two-bedroom rental apartments of up to 100 sq m in size;

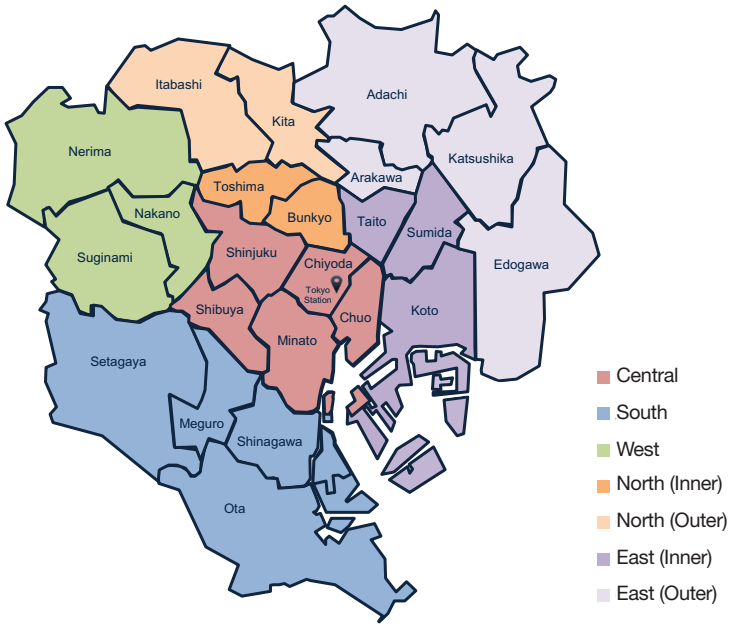
2) reinforced concrete structures built within the last ten years; and

3) properties located in Tokyo's 23 wards and situated within a ten-minute walk of the nearest station.

In contrast to the luxury residential market, advertised or 'asking' rents for mid-market units fitting the above criteria are typically non-negotiable and are not subject to incentives such as rent-free periods. Savills mid-market rental indices are therefore considered to closely reflect movement in contract rents for the Tokyo market.

MAP 1

Tokyo's 23 wards delineated by survey area



Source: Savills Research & Consultancy

Rents in Tokyo's 23 wards softened slightly in Q3/2016 after impressive Q2 gains driven mainly by newly completed apartments in the central five wards. The city's current trend of slow, gradual increases is not expect to significantly change. At the time of writing, rents are still up YoY in 17 of the city's 23 wards, and QoQ fluctuations are primarily limited to Shinjuku and Chiyoda.

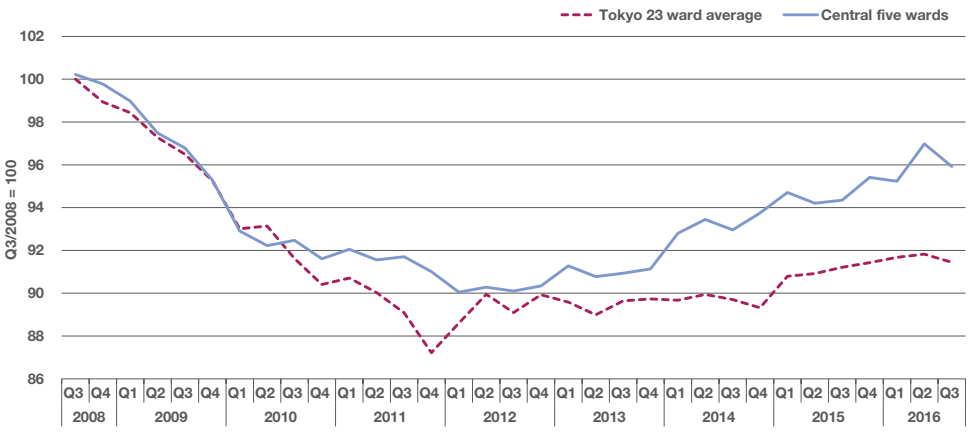
In Shinjuku, Sumitomo opened its high-end La Tour residence in March, which was actively leasing throughout Q2 and drove the ward's rental index up 3.5% last quarter. A similar effect occurred in Chiyoda Ward, which saw the opening of Miraizu Residential Kudan, a centrally-located 13F apartment building. Leasing has slowed in Q3 as both approach capacity.

The current average rent in Tokyo's 23 wards stands at JPY3,624 per sq m, still 8.6% below 2008 levels. This average represents a 0.4% decrease QoQ and a 0.3% increase YoY.

Rents in the central five wards have bounced back with more strength, despite their temporary retreat, and are currently 4.1% below their 3Q/2008 base. In Q2/2016 alone rents increased an average of JPY77 per sq m or 1.8% over the preceding quarter, the single highest quarterly increase since the crisis.

GRAPH 1

Tokyo mid-market apartment rental index, Q3/2008–Q3/2016



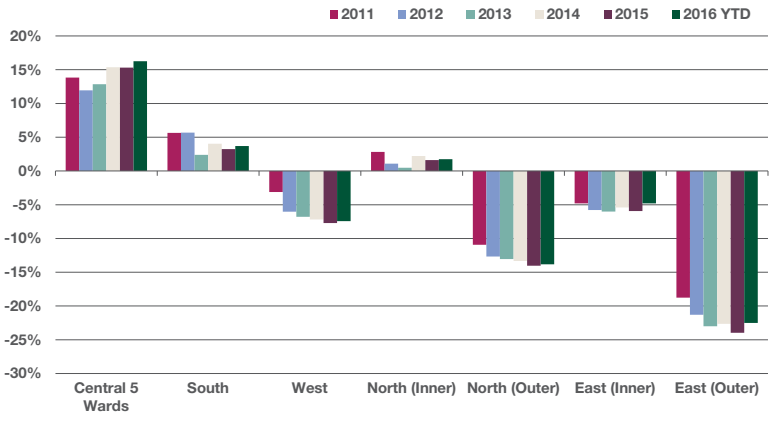
Source: Savills Research & Consultancy

Tokyo mid-market rental trends by survey area

Graph 2 shows the differences in rental levels between the Tokyo 23-ward average and each area as a rental premium (%) for each year. For example, a positive figure depicts the extent to which the area's rental

GRAPH 2

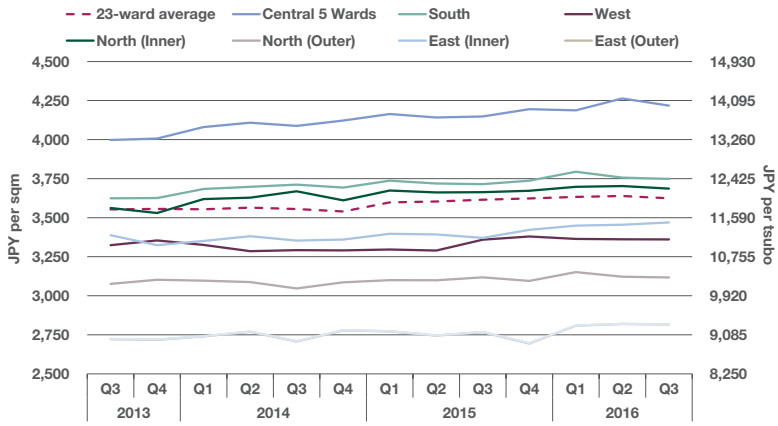
Rental premiums and discounts over the Tokyo 23-ward average, 2011–Q3/2016



Source: Savills Research & Consultancy

GRAPH 3

Average asking rents for mid-market rental apartments by survey area, Q3/2013 – Q3/2016



Source: Savills Research & Consultancy

level is higher than the Tokyo 23-ward average.

In general, centrally located areas such as the central five wards and their adjacent neighbourhoods show higher rental premiums due to their convenience and accessibility. Outer areas, such as Outer North and Outer East, tend to have discounts.

As of Q3/2016, the highest premium was observed in the central five wards at 16.3%. The South and the Inner North recorded positive premiums of 3.7% and 1.7% respectively. The outer areas, meanwhile, showed discounts. The greatest discount was seen in the Outer East area at -22.5%, followed by Outer North at -13.7% and West at -7.5%. The Inner East area – comprised of Koto, Sumida and Taito wards – currently shows a discount of -4.8% and has been catching up to the 23-ward average.

The central five wards have gradually pulled away from the city average over the past five years, seeing modest increases in premium almost every year. The other wards, by contrast, appear to be flattening somewhat as they slowly converge toward the average at a rate of approximately 0.1ppt per quarter.

The central area is up 1.7% YoY as of Q3/2016, now in third place after a brief stint at the lead of the pack in Q2 in YoY terms. It has been surpassed by growth in the Inner East and Outer

TABLE 1

Average monthly asking rents by unit size, Q3/2016

Size band	15–30 sq m		30–45 sq m		45–60 sq m		60–75 sq m	
Survey area	JPY per sq m (tsubo)	% QoQ	JPY per sq m (tsubo)	% QoQ	JPY per sq m (tsubo)	% QoQ	JPY per sq m (tsubo)	% QoQ
Tokyo's 23 wards	3,680 (12,165)	-0.5	3,530 (11,670)	-0.5	3,500 (11,570)	0.2	3,510 (11,605)	-3.5
Central five wards	4,360 (14,415)	-0.1	4,090 (13,520)	-1.6	4,110 (13,585)	0.2	4,070 (13,455)	-2.2
No. of units surveyed	>5,000		>5,000		>2,500		>500	

Source: Savills Research & Consultancy

East areas, which are up 2.9% and 1.8% YoY respectively. The Inner East area has been gradually catching up to the city average in recent quarters, perhaps due to its convenient accessibility to business districts and new commercial developments around Tokyo Station. The Outer East area, meanwhile, remains the most affordable area in the city, magnifying the YoY percent impact of rental changes. Current average rents stand at JPY3,469 per sq m (JPY11,468 per tsubo) in the Inner East area and JPY2,816 per sq m (JPY9,309 per tsubo) in the Outer East area.

Tokyo mid-market apartment rents by unit size

Tokyo's rental market is principally made up of compact single-occupier units, typically less than 45 sq m (13.6 tsubo) in size. Unlike other major global cities such as London and New York, house or apartment sharing does not form a major segment of the rental market. As a result, there is a large, stable market for small- to mid-sized units.

Table 1 shows that in Q3/2016 Tokyo's smaller single rooms (15-30 sq m) and average family units (45-60 sq m) were most resilient. Larger single units and larger family size units saw small corrections, though a lack of data for units over 60 sq m can result in more variability. Apartments in the 60-75 sq m range in the 23 wards saw a gain of 4.0% in Q2, for example, against a decline of -3.5% in Q3.

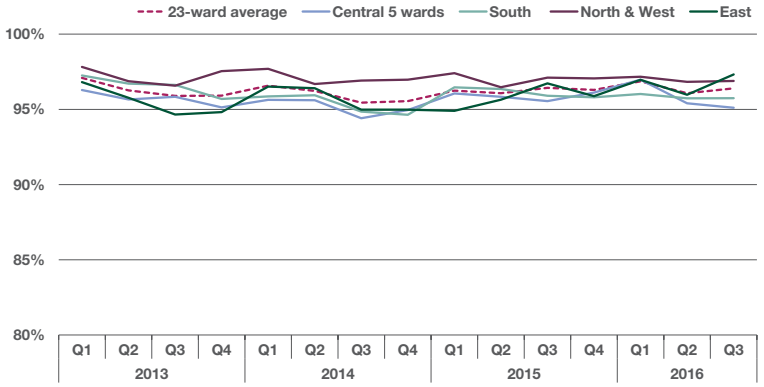
Rents for 15-30 sq m units averaged JPY3,680 per sq m (JPY12,165 per tsubo) in the 23 wards as a whole and approximately 700 yen higher at JPY4,360 per sq m (JPY14,415 per tsubo) in the central five wards specifically. As is typical, larger units lease for lower per-sq m prices, seeing discounts of about 4-5% per sq m in Tokyo as a whole and 6-7% in the central five wards.

Occupancy rates

Average occupancy rates in Tokyo recovered after a slight decline in Q2/2016, rising to 96.4% in the 23 wards in Q3/2016. The increase was most visible in the eastern areas, which partially explains their relatively strong rental increases for the year.

GRAPH 4

Average occupancy rates for J-REIT residential assets, Q1/2013–Q3/2016



Source: Savills Research & Consultancy based on publically disclosed J-REIT* property data (* Advance Residence and Nippon Accommodation Fund)

GRAPH 5

New housing starts in Tokyo Prefecture by use, 2005–2015

Source: Tokyo Metropolitan Government, Savills Research & Consultancy

In YoY terms the average occupancy rate for Tokyo's 23 wards was almost perfectly flat, declining just 4 basis points. Movements in other survey areas were subdued, each moving fewer than 100 basis points YoY. Tokyo occupancy remains strong in general, and it has been a full year since any survey area dipped below 95%. The highest occupancy rate was recorded in the Outer East area at 97.5%, while the lowest was in the central five wards at 95.1%.

The Outer East area's improvement puts it above the North and West areas, which have until this quarter shown the highest occupancy rates since the financial crisis.

Housing supply analysis

Following a pattern similar to most other major urban centres, new housing starts in Tokyo Prefecture peaked at almost 190,000 units annually in 2005 and 2006 before abruptly dropping after the global financial crisis. After bottoming out at 108,000 in 2009, new housing starts have since climbed back to settle at about 140,000 units annually in the prefecture and 110,000 in the 23 ward area (the 23 wards typically comprise 75% of the prefectural total). New construction has held steady at this level for almost half a decade. Considering that Tokyo Prefecture has added about 100,000 new registered households on average annually over the decade, and also factoring in demolitions, 140,000 new housing starts a year appears to be close to equilibrium with demand.

There is a small but noticeable trend toward providing rental units and

away from providing other types of housing since 2011. In that year rental units made up 37% of new housing starts; the figure has climbed steadily to 45% in 2015. This partially reflects increased developer appetite for selling rental units to retail investors. Such a trend illustrates increasing popularity for rental units in Tokyo both among occupiers and investors. Even Mitsubishi Estate began offering one-room units for investors in late May.

OUTLOOK

The prospects for the market

Q3/2016 marks the first quarterly correction in the 23-ward average since 2014, though it was primarily driven by new high-end buildings opening in Q2. Underlying fundamentals remain solid – occupancy continues to hover above 95%, population growth is progressing, and even real wages have grown seven consecutive months – further indicating that this is more likely a temporary adjustment. Property prices have grown significantly over the past few years, but it appears that rents still need more time to pick up.

Considering that rents are still several percentage points below their pre-crisis peaks, and the stable nature of the underlying Japanese economy, gradual rental growth is expected to continue into the future even if we see a correction or two along the way.

Please contact us for further information

Savills Japan

Christian Mancini
CEO, Asia Pacific
(Ex Greater China)
+81 3 6777 5150
cmancini@savills.co.jp

Savills Research

Tetsuya Kaneko
Director, Head of Research
& Consultancy, Japan
+81 3 6777 5192
tkaneko@savills.co.jp

Hafiz Ismail
Manager, Research &
Consultancy, Japan
+81 3 6777 5171
hismail@savills.co.jp

Simon Smith
Senior Director
Asia Pacific
+852 2842 4573
ssmith@savills.com.hk